

# STATE FISCAL NEEDS AND INTERSTATE COMMERCE

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When the Constitution of the United States was framed in 1787 commerce between the states accounted for a minor part of the business activity within the new nation. Multistate enterprises, so numerous today, then were virtually unknown. Improved means of transportation and of communication, together with the development of mass production, have wrought major changes in the economy.

Now interstate commerce constitutes a large share of the nation's business. Each year it becomes increasingly important that those engaged in this type of commercial activity pay their proportionate share of the expense of government. As the United States Supreme Court has observed,<sup>1</sup> business is not done in a vacuum. The market for the products that are sold in interstate commerce is made possible by an organized society which, to a large extent, exists as a result of the expenditures of state and local governments.

No state or local tax official should question the wisdom of the framers of the Constitution when they wrote the commerce clause.<sup>2</sup> What was done in this regard 170 years ago must be recognized as the foundation upon which our national unity has been built. Those who engage in interstate commerce must be assured that they shall not be the objects of discrimination by the states or their political subdivisions. Misguided local interest could produce havoc. Wisely has the Congress been given the power to regulate commerce between the states.

But it was not the purpose of the commerce clause to relieve those engaged in interstate commerce of their just share of state tax burdens, merely because an incidental or consequential effect of the tax is an increase in the cost of doing business. Not all state taxation is to be condemned because, in some manner, it has an effect upon commerce between the states, and there are many forms of tax whose burdens, when distributed through the play of economic forces, affect interstate commerce, which nevertheless fall short of the regulation of the commerce which the Constitution leaves to Congress.<sup>3</sup>

No better statement of the position of a state tax official on this important aspect of his work could be made than the expression of Mr. Justice Stone that has just been quoted. Interstate commerce should pay its way, but it should not be subjected to discriminatory burdens. In essence, then, the government viewpoint is that concerns engaged solely

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<sup>1</sup> James v. Dravo Contracting Co., 302 U.S. 134 (1937).

<sup>2</sup> U. S. Const., art. 1, §8.

<sup>3</sup> McGoldrick v. Berwind-White Coal Mining Co., 309 U.S. 33, 46 (1940), citing Western Live Stock v. Bureau of Revenue, 303 U.S. 250 (1938).

in interstate commerce should share in the cost of state and local government along with those whose business is solely intrastate or both interstate and intrastate. There should be no discrimination against interstate commerce but neither should it enjoy a preferred position to the detriment of other business.

Years of contact with taxpayers give rise to the conviction that they share this view. No one really enjoys paying taxes, but everyone realizes that they must be paid if we are to have the governmental benefits that make our economy possible. Really strong objection to the taxing process is usually traceable to the belief that more than a fair share of the tax burden is being exacted. It becomes important, then, to examine the revenue needs of the states, the economic and administrative limitations encountered in meeting those needs, and the impact of the commerce clause upon state tax structures. Finally, there is need to evaluate the economic soundness of tests that are applied under the commerce clause to determine whether or not state taxes contravene its provisions. Are we sacrificing form to substance? If so, it is more than likely that the results are unfair, sometimes to interstate commerce and at other times to intrastate commerce. What are the best means available to us under the law to achieve our goal of fairness to both?

#### INCREASING NEED OF STATE REVENUE

At the outset it should be observed that state revenue needs are pressing. New conceptions as to what government shall do for the people require new conceptions as to what the people shall do to sustain the government. Increasing activities of government and widespread extension of its benefits necessitate re-examination of economic concepts formed during periods when governmental services were not so universally enjoyed.

Prices continue to rise. Save in a few states populations are growing; in some states at very rapid rates. Not only are the services which states are expected to render expanding, but they are also becoming more costly. The problem is a grave one. The Governor of Kentucky entitled a speech that he gave in 1953 before the National Tax Conference "Fiscal Crisis in the States". He cited as the basic cause of this crisis "the great growth of governmental expenditures at all levels."<sup>4</sup>

Compilations of the U. S. Bureau of the Census give proof of the steady increase in state expenditures during the postwar years. From a total expenditure of state governments in 1944 of slightly over \$5 billion<sup>5</sup> the amount has risen constantly to a corresponding total in excess of \$20 billion for fiscal 1955.<sup>6</sup> This represented a percentage in-

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<sup>4</sup> National Tax Association Proceedings, 1953, p. 291.

<sup>5</sup> Revised Summary of State Government Finances, 1942-1950, United States Department of Commerce, Bureau of the Census, (1953) p. 5.

<sup>6</sup> Compendium of State Government Finances in 1955, United States Department of Commerce, Bureau of the Census (1955), Table 1, p. 6.

crease of 294 in the period from 1944 to 1955.<sup>7</sup> There is no indication that there will be any decrease in the amount of expenditures, or for that matter even in the annual rate of increase therein, since demands are being made continually for more highways, education, welfare, and other governmental services.

State tax collections have also risen constantly in this postwar period. Between 1944 and 1955 there was an increase of 185 percent, from \$4.1 billion to \$11.6 billion.<sup>8</sup> In 1956, despite these earlier increases, the rate of gain over 1955 was a startling 15 percent.<sup>9</sup> These statistics are a reflection of the growing demands for governmental services. They demonstrate the ever-increasing need for revenue to pay for these services.

#### PRESENT LIMITATIONS ON REVENUE YIELDS OF VARIOUS TAXES

Recognition must be given to the economic and administrative limitations upon the ways in which the states may meet these revenue needs. Under our federal system the national government is paramount. Its demands represent a much larger proportion of the tax dollar than do those of the state and local governments. There is only one set of taxpayers to respond to the requirements of all of these governments. Hence the states are not free to find solutions to their revenue problems unimpeded by the complication that the same taxpayers will have also to pay federal taxes out of the same sources. Out of such a situation arise both economic and administrative limitations in the development of sound tax structures.

*Economic.* Although it is difficult to come to positive conclusions as to the percentage of the gross national product that can be taken by the governments through taxation without ultimately impairing the economy, it seems to be generally agreed that care must be taken in the United States if we are to avoid such a danger. Barring only World War II, our taxes are at their highest levels in history. When Colin Clark asserted recently that there is a 25 percent limit<sup>10</sup> his views were warmly echoed in many quarters. His thesis is that tax increases become self-defeating when that limitation is exceeded. He says that taxes beyond this point impair the incentives to work and invest, and weaken employers' resistance to wage increases and wasteful business spending. Although these ideas have gained wide attention, there has been no general acceptance of the assertion that 25 percent of our national income is the limit beyond which taxes cannot go without inviting disaster.

Even those who do not agree with Mr. Clark concede that there

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<sup>7</sup> *Id.*, Table 39, p. 54.

<sup>8</sup> See publication cited in note 5, *supra*, at p. 4 and publication cited in note 6, *supra*, at p. 6.

<sup>9</sup> State Tax Collections in 1956, United States Department of Commerce, Bureau of the Census, Table 1, p. 3.

<sup>10</sup> Clark, *Public Finance and the Value of Money*, Economic Journal, December 1945; *The Danger Point in Taxes*, Harper's Magazine, December 1950.

are economic limits to taxation. Speaking at the National Tax Conference in 1952, Professor Walter W. Heller, of the University of Minnesota, addressed himself to the subject "How High Can Taxes Go?"<sup>11</sup> He pointed out that it is increasingly recognized that taxable capacity can be assessed only in terms of several quantitative and qualitative factors. In this connection six were enumerated: (1) the level and composition of government expenditures; (2) the size and distribution of a national income; (3) the nature of economic modification and flexibility of private economic action; (4) the composition of the tax system and the structure of particular taxes; (5) the state of the art and science of tax administration and its translation into practice; and (6) the degree of taxpayer resistance to, or acceptance of, tax measures.

In his analysis of these factors Professor Heller started with reference to the one last enumerated, *viz.*, taxpayer resistance. He noted that this is closely interrelated with several of the other limiting factors. He added: "It is also tied to tax structure in administration in terms of taxpayer confidence in the fairness of the tax system and the evenhandedness of its administration." Finally, he observed: "The pains of taxation are highly personal and individual and hence keenly felt by the taxpayer. The benefits, in contrast, are largely impersonal and collective and hence only dimly seen. . . . Small wonder, then, that the political *will* to tax runs out considerably sooner than the economic *capacity* to tax." In the light of these conditions it may readily be seen that the states are confronted by a problem for which there is no easy answer.

Even though it may appear that the economic limit of taxation has not been reached, state legislatures are often dissuaded from providing badly needed funds through taxation because of the pains of taxation which are so keenly felt by their constituents. When states are competing for population or industry, questions are frequently raised as to whether taxes may not discourage business from coming into a state. Those who have studied the matter have indicated that the importance of taxes as a factor in such decisions may have been overrated, but nonetheless the questions persist.<sup>12</sup>

*Administrative.* Another limitation upon revenue yields that plagues the states is the fact that they must eschew taxes that involve excessive administrative expense or which, although normally self-assessed, are so complicated as to discourage taxpayers from making accurate returns. For example, if a state is precluded from imposing a sales tax because a transaction is in interstate commerce, frequently it is not feasible to offset this by providing for a use tax payable by the consumer when the interstate movement of the property has ended. Many transactions of this kind are too small and too irregular to be made the subject of audit or

<sup>11</sup> National Tax Association Proceedings, 1952, p. 243.

<sup>12</sup> Floyd, *The Effect of State and Local Taxes upon the Selection of Industrial Locations*, National Tax Association Proceedings, 1951, p. 435; Garwood, *Taxes and Industrial Location*, 5 National Tax Journal 365 (1952).

investigation by the administrative agency without incurring expense that is disproportionately high. Moreover, the problem of acquainting potential use tax payers with the operation of such a law admits of no easy solution.

Even if the average user of property that has been acquired by him as a result of an interstate transaction were aware of a resultant use tax obligation, compliance with the law would be a distasteful and complicated chore. He would need to keep accurate records of all such purchases and to be prepared to account for them through the filing of periodic returns with the tax administrator.

Experience has shown that where such obligations accrue more or less intermittently and in relatively small amounts there is no practical means of enforcing the application of a use tax. Both from the standpoint of the taxpayer and of the tax administrator, the record keeping complications seem to have been regarded as too great to warrant trying to make the use tax of as universal application as a strict reading of the law might indicate. Individually these transactions may seem insignificant, but there are undoubtedly many of them. In the aggregate they must represent a substantial volume of trade that is competitive with comparable transactions in intrastate commerce as to which sales taxes are paid by the retailers who secure reimbursement therefor from their customers.

Here, then, is another limiting factor upon a state government that seeks to meet its revenue needs by way of a sales tax applicable to intrastate transactions, but which, because of the commerce clause, cannot apply the same tax to interstate business.<sup>13</sup> So long as the rate of the sales tax is such as to result in no significant disadvantage to the local retailer, the state may employ this method of taxation without serious repercussions. But once the retailers find that business that would otherwise be theirs is being diverted out of state to avoid the economic burden of the sales tax, objection to this means of raising revenue will constitute a serious problem for state lawmakers. Not only will the sales tax be self-defeating by curtailing the amount of business to which it is intended to apply, but it will also affect adversely the property values and income that are used to measure other tax obligations under state law. The conclusion is inescapable, therefore, that the commerce clause imposes very real economic and administrative limitations upon the nature and extent of state tax structures.

This is not to say that the use tax cannot be employed successfully by a state government to cope with the problems rising out of the purchase of property in another state for use in the taxing jurisdiction.<sup>14</sup> When the items of property are of a kind that must be registered with

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<sup>13</sup> See *A. Magnano Co. v. Hamilton*, 292 U. S. 40 (1934).

<sup>14</sup> *Henneford v. Silas Mason Co.*, 300 U.S. 577 (1937); *Southern Pacific Co. v. Gallagher*, 306 U.S. 167 (1939).

some public agency, as for example motor vehicles, it is feasible for the tax administrator to be informed of their arrival and use in his state. The amount of tax involved is sufficiently large to warrant the time and effort required to effect its collection directly from the user.<sup>15</sup> Similarly, when large items of mechanical equipment or building materials have been purchased elsewhere for in-state use, the tax administrator is reasonably successful in learning of this and in following through with the enforcement of the law.

Then, too, interstate transactions are made frequently by sellers who maintain places of business in the state where the use occurs. In such instances these vendors may be required to collect the use tax from their customers for the benefit of the state,<sup>16</sup> thus overcoming the difficulties that otherwise would confront the tax administrator if he had to secure individual consumer use tax returns from each of these purchasers.

Perhaps the advantage accruing to a state government in a situation of this kind may best be illustrated by drawing a comparison with the experience in federal income tax administration. No one would question seriously the great advantage enjoyed by the Internal Revenue Service through the collection of income taxes by means of withholding the estimated liability of an employee from wage or salary payments. In much the same way a state may enforce its use tax with respect to an interstate transaction, avoiding complications that otherwise might make the tax a much less effective source of revenue. Unlike the Federal Government, however, the state may employ this means only when the vendor is subject to its jurisdiction as a result of having a place of business within the state or has voluntarily undertaken to collect the tax even though maintaining no such outlet within the state. If some practical method could be found to enable states to enforce use taxes more widely through collections made by vendors, much of the difficulty that has been experienced in state sales and use tax administration because of commerce clause limitations upon the taxing power would disappear. No solution is readily available, but some indication of what might be done may be had from the experience gained in the administration of state gasoline taxes.

When Oregon passed the first motor vehicle fuel tax in 1919, its example was soon followed by other states. Finally the tax became one of universal application throughout the nation. Large quantities of gasoline move in interstate commerce. It is important for the states concerned to have knowledge of these shipments and to be assured that when the fuel is sold the proper state tax is paid. At first there was considerable difficulty in securing these data, but the oil companies and the state tax administrators soon recognized the need for cooperative

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<sup>15</sup> In California, for example, the revenue from the 3 percent use tax applicable to motor vehicles bought out of state amounted to \$2,286,000 for the year ended June 30, 1956. Some 31,600 vehicles were involved.

<sup>16</sup> *Felt & Tarrant Mfg. Co. v. Gallagher*, 306 U.S. 62 (1939).

action. Today the state into which gasoline is shipped in interstate commerce is supplied with the facts concerning the shipment and is prepared to follow through effectively with the enforcement of its tax. It is enabled to do this through the cooperation of the state of origin, as well as of the oil companies concerned. The needs of the consumers are met without complications and without the possibility of disruption of trade that would inevitably result if more than one state should attempt to impose a gasoline tax on the same fuel.

Although the conditions under which general sales and use taxes are imposed by states are by no means entirely apposite, the experience in gasoline tax administration should prove helpful in meeting the problems of sales and use taxes arising out of interstate transactions. The same ingenuity that enabled tax administrators and the sellers of gasoline to solve their problems could do much to ameliorate like difficulties experienced in the general sales tax field. When a retailer makes a sale in interstate commerce, it is normal for him to claim exemption in the state of origin and not to pass on any tax reimbursement to his customer in the other state. Both states may have sales and use taxes, and transactions of this type may occur in both directions. Perhaps an extension of the same techniques used so successfully in connection with the gasoline tax would prove feasible.

Some modification of procedures would doubtless be required because of differing circumstances. There are many more vendors concerned with sales taxes than gasoline taxes. In one instance a great variety of products is involved, whereas in the other only a single commodity is affected. But it is believed that these differences do not present insuperable barriers to a solution. Once the states are agreed, as seems to be rather generally the situation now, that the revenue accruing with respect to an interstate transaction should go to the state where the property is to be used, suitable means could be developed to assure that result. Then the interstate commerce would pay its fair share of the tax, but would not be unfairly treated by any attempt on the part of both states to derive revenue from a tax measured by the amount involved in the same transaction. If congressional assistance should be needed to make this workable, that might be given subject to the assurance that the states treat interstate transactions with absolute impartiality and would refrain from imposing on them burdens that are in any way heavier than those on comparable intrastate trade.

No attempt will be made here to set forth the details of such a plan, as that would be a project beyond the scope of this article. It is confidently predicted, however, that if sales and use taxes continue to constitute such an important part of the revenue structures of the states there will be developments along the lines that have been indicated. The drafting of the necessary legislation, both state and federal, to make this possible presents a real challenge to those who recognize that the law should be made to serve, not to impede, the economy.

IMPACT OF COMMERCE CLAUSE UPON SELECTION  
OF TYPES OF TAXES

Do the cases decided under the commerce clause influence the selection of types of taxes by the states? It seems clear that they do. The use tax has already been mentioned. It was developed because of the restricted scope permitted to the sales tax under the decisions.<sup>17</sup> In effect the United States Supreme Court has required the states to select certain types of taxes and to give them approved appellations.

Cases illustrating that the name given to a tax is important are *McLeod v. J. E. Dilworth Co.*,<sup>18</sup> in which the court held that Arkansas could not collect a sales tax when the order was solicited by a drummer in that state for acceptance in Tennessee by the seller, who then shipped the goods directly to the buyer, and *General Trading Co. v. State Tax Commission*,<sup>19</sup> decided the same day, in which the court upheld the application of the Iowa use tax to property acquired through a substantially identical transaction. In a later case, *Spector Motor Service, Inc. v. O'Connor*,<sup>20</sup> the court stressed this type of distinction when it said, "Even though the financial burden on interstate commerce might be the same, the question whether a state may validly make interstate commerce pay its way depends first of all upon the constitutional channel through which it attempts to do so."

To achieve equality of tax treatment for interstate and intrastate business, and at the same time to comply with these restrictions, a state may be compelled to tax interstate business under one law while intrastate business is taxed under another law. Thus, in California, corporations are taxed with respect to their net income under two different provisions, depending upon whether or not they do any intrastate business within the jurisdiction.<sup>21</sup> If only interstate business is done the tax is imposed directly upon the allocable net income which is exclusive of income exempt from direct taxation. On the other hand, if a corporation is engaged in some intrastate business the tax is inclusive of income from tax-exempt sources and is denominated a "franchise" tax. A corporation engaged exclusively in interstate commerce is favored, although the tax advantage that it receives may be small. At least, it does pay a tax at the same rate on that portion of its taxable income allocable to California that is paid by another corporation with respect to its income from intrastate business.

It seems inevitable that the limitations resulting from the commerce clause upon the power of a state to impose taxes with respect to interstate business operate restrictively upon the taxation of intrastate

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<sup>17</sup> *Gregg Dyeing Co. v. Query*, 286 U.S. 472 (1932).

<sup>18</sup> 322 U.S. 327 (1944).

<sup>19</sup> 322 U.S. 335 (1944).

<sup>20</sup> 340 U.S. 602, 608 (1951).

<sup>21</sup> Cal. Revenue and Taxation Code, §§23151 and 23501. See *West Publishing Co. v. McColgan*, 27 Cal. 2d 705, 166 Pac. 2d 861, affirmed 328 U.S. 823 (1946).



activity. As has been observed, mass production and improved facilities for the transportation of goods, as well as for communication, have made interstate commerce a potent factor in our economy. If a state is unable to lay a tax with respect to interstate business the wisdom of doing so with respect to competitive intrastate business may well be questioned. The expression, "interstate commerce must pay its way", is more than a mere form of words. It is the statement of an economic principle applicable to the tax structure of a state.

If interstate commerce does not pay its way, then intrastate commerce may be placed at a serious disadvantage, the relief of which requires that similar tax immunity be extended. But the rising costs of government must be met, and the state that attempts to temper the wind to the shorn lamb may find itself in an untenable position. It will be confronted with a fiscal crisis of the type so vividly described by Governor Wetherby of Kentucky when the National Tax Conference met in his Commonwealth in 1953.<sup>22</sup>

#### EVALUATION OF ECONOMIC SOUNDNESS OF COMMERCE CLAUSE TESTS

As has been indicated, the evaluation of the economic soundness of the commerce clause tests must be in terms of whether they prevent the states from getting a just portion of their revenue from enterprises engaged in interstate commerce.<sup>23</sup> If interstate business does not pay its fair share of the cost of the state governments when such a test is applied, then it cannot be said that the test is economically sound.

Perhaps the most disturbing aspect of the whole matter is the continuing uncertainty concerning the validity of the application of state tax laws to interstate activities. The restrictive nature of the tests under the commerce clause is bad enough, but the additional problems created by this persistent uncertainty are even worse. It would be extremely helpful in framing and administering state tax laws if there were a surer guide as to what may be done toward requiring interstate commerce to pay its own way.<sup>24</sup> Laws that comport with the concept of fairness as applied to intrastate business, all too often run afoul of tests applied thereto in the interpretation of the commerce clause when the states endeavor to secure thereunder what they believe to be a fair share of the revenue from interstate activity. If the most equitable means of

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<sup>22</sup> *Supra*, note 4.

<sup>23</sup> Because of the constant pressure for revenue with resultant higher taxes, if states do not derive a fair share of their revenues from interstate business, the adverse effect upon competitive intrastate activity becomes increasingly severe with bad economic consequences.

<sup>24</sup> The difficulty confronting the states is succinctly stated in 51 Am. Jur. 263 thus: "Almost every tax imposed by a state in some degree affects interstate commerce, and whether a tax affects such commerce to an unconstitutional extent is largely a question of degree depending upon the facts in each case."

taxing such business are not to be permitted under these tests, the states can enact reasonable alternatives, but if their governments are left in the dark they proceed at their peril. The situation may become extremely aggravated when, after lengthy litigation, states find that they have no income at all from this source for many years so far as interstate commerce is concerned. This was recognized in the *Spector* case dissent in these forceful terms.<sup>25</sup>

It has taken eight years and eight courts to bring this battered litigation to an end. The taxes involved go back thirteen years. It is therefore no answer to Connecticut and some thirty other states who have similar tax measures that they can now collect the same revenues by enacting laws more felicitously drafted. Because of its failure to use the right tag, Connecticut cannot collect from *Spector* for the years 1937 to date, and it and other states may well have past collections taken away and turned into taxpayer bonanzas by suits for refund not barred by the respective statutes of limitation.

Nor can the states be entirely certain that statutes recast in the light of this decision will be immune from later constitutional attack.

As the *Spector* case illustrates, the court has inclined toward a formalistic approach. Under this, various tests have evolved in each of the areas of state taxation. The economic soundness of each test must be examined separately. In the final analysis, it can be said, however, that no test is economically sound if it either allows interstate commerce to avoid its fair share of taxes or requires it to pay more than that share. It is submitted that the very reason for the presence of the commerce clause in the Constitution is to prevent disruption of the economy through singling out commerce between the states for tax treatment that does not comport with what is done in respect to other business. Whenever interstate commerce is permitted to avoid its fair share of the expense of government it gains a competitive advantage that will result in an uneconomic distribution of goods. Conversely, if state taxes discriminate against interstate commerce the same undesirable results must be anticipated. In either event the tests cannot be regarded as economically sound, and if this is true, their validity is subject to serious question. It is becoming increasingly important that the sound development of our economy shall not be impeded by unequal tax treatment of interstate and intrastate trade.

These are general considerations. To evaluate the tests as applied to specific areas of state taxation it is necessary to consider each separately. In the eight brief paragraphs that follow, this is done, by no means exhaustively, but in such a way as to illustrate the problems that are involved.

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<sup>25</sup> 340 U.S. 602, 614 (1951).

1. *Taxes on Property.* The court asks: are the goods in transit? If they are, the state cannot impose an *ad valorem* property tax.<sup>26</sup> If not, it can.<sup>27</sup> The soundness of this is debatable. Under the prevalent "tax day" system some goods escape all taxes while others are taxed twice. It should be possible to develop a more satisfactory test that would assure occurrence of neither of these eventualities.

2. *Taxes on Instrumentalities of Interstate Commerce.* The court allows the states to tax these if a tax is fairly apportioned to the time the property is within the taxing state.<sup>28</sup> On the surface this test appears to be practical and sound, but there is always a possibility that this property may be taxed at more or less than 100 percent due to the use of different formulae in determining the shares of the respective states. Thus, a test that is basically sound may be found to operate unfairly. The need for development of the law to prevent this is indicated.

3. *Sales and Use Taxes.* The Supreme Court allows the state of situs (place of sale or use) of the transaction to impose the tax.<sup>29</sup> This test is fallible. It can result in two different states actually taxing the same economic value through a formalistic approach which attributes to the state of sale the right to impose a tax on that event measured by the price of the goods, and at the same time permits the state of use to impose a like tax measured by the same price. Under such circumstances interstate commerce is at a disadvantage because states do not normally impose both taxes on a comparable intrastate transaction. It is suggested that passage of title has little or no bearing on the question of how the revenue from an interstate transaction of this kind should accrue. The weight of opinion seems to support the view that the tax should be imposed by the buyer's state only. This would appear to be a sound economic test, but there is need for development of the law to permit of its application as a practical matter.

4. *Gross Receipts Taxes.* These are allowed to apply to interstate business *only* if fairly apportioned to clearly local activities.<sup>30</sup> Both from economic and legal standpoints, this appears to be a good test. There seems to be no need for revision of approved tax procedures in this area of the law in order to achieve the goal that interstate commerce shall pay its way, no more, no less.

5. *Net Income Taxes.* Following the decision in the *West Pub-*

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<sup>26</sup> *Bacon v. Illinois*, 227 U.S. 504 (1913).

<sup>27</sup> *Minnesota v. Blasius*, 290 U. S. 1 (1933); *Empresa Siderurgica, S. A. v. Merced County*, 32 Cal. 2d 68, 194 Pac. 2d 527, affirmed 337 U.S. 154 (1949).

<sup>28</sup> *Nashville, Chattanooga & St. Louis Ry. v. Browning*, 310 U.S. 362 (1940); *Braniff Airways v. Nebraska State Board*, 347 U.S. 590 (1954).

<sup>29</sup> *General Trading Co. v. State Tax Commission*, 322 U.S. 335 (1944); *Norton Co. v. Department of Revenue*, 340 U.S. 534 (1951).

<sup>30</sup> *Canton R. Co. v. Rogan*, 340 U.S. 511 (1951); *Central Greyhound Lines v. Mealey*, 334 U.S. 653 (1948); *J. D. Adams Mfg. Co. v. Storen*, 304 U.S. 307 (1938).

lishing Co. case, approving this type of taxation as applied to interstate business where there is a fair apportionment of income to sources within and without the state, it might have been assumed that a clear test had been adopted.<sup>31</sup> Some doubt has now been created concerning the test since the *Spector* decision, which seemed to reach an opposite result under closely analogous conditions. Among those who work in the field of taxation, both as counsel for tax administrators and as the representatives of taxpayers, a fairly apportioned tax on the net income of an interstate activity is generally regarded as one of the best means of requiring that business to pay its own way. There seems to be no compelling reason why one who is engaged in interstate commerce should not be subject to such a tax so long as the rates are not "rigged" to effect a discrimination against him and to accord more favorable treatment to intrastate commerce.

6. *Drummer and Peddler Taxes.* As to taxes of these types the rule that has been frequently repeated is that a peddler tax is valid if nondiscriminatory, while a drummer tax is invalid as inherently discriminatory.<sup>32</sup> Application of such a test often provokes controversy. It is believed that if the validity of the tax in either situation turns upon whether its application is discriminatory a much more satisfactory result would be obtained. A conclusion that a tax on a drummer engaged in interstate commerce is inherently discriminatory seems difficult to justify. It may or may not be, depending upon the circumstances, and these should be as readily demonstrable as they are in connection with a tax upon peddlers.

7. *Highway Taxes.* In this field of law pertaining to the taxation of interstate commerce there have been what may be described as the most heartening developments. Such taxes have been held valid if they are nondiscriminatory and fairly related to the benefits received.<sup>33</sup> Certainly this represents a realistic approach to the problem of how an interstate business should be taxed when it benefits, along with its intrastate counterpart, from the use of facilities furnished by the state. Some of the approaches to the problem of arriving at a fair apportionment of highway user taxes have left much to be desired, but there are indications that means are available to the states to solve the problem in a fair and practical manner within the framework of the test prescribed by the court.<sup>34</sup>

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<sup>31</sup> See *supra*, note 21 and *United States Glue Co. v. Oak Creek*, 247 U. S. 321 (1918). But see *Spector Motor Service, Inc. v. O'Connor*, 340 U.S. 602 (1951).

<sup>32</sup> See *Memphis Steam Laundry Cleaner, Inc. v. Stone*, 342 U. S. 389 (1952); *Robbins v. Shelby County Taxing District*, 120 U.S. 489 (1887), *Caskey Baking Co. v. Virginia*, 313 U.S. 117 (1941).

<sup>33</sup> *Capitol Greyhound Lines v. Brice*, 339 U.S. 542 (1950).

<sup>34</sup> The National Association of Tax Administrators and the Council of State Governments have made proposals that are designed to accomplish fair apportionment of highway user taxes affecting interstate operations. See *A Practi-*

8. *Privilege of Engaging in Interstate Commerce.* Any state tax on this privilege appears to be *ipso facto* void.<sup>35</sup> A levy of this type has been characterized as an attempt on the part of the state to invade a field of regulation reserved to the Congress, and as such prohibited to the states. Is it necessary to adopt such a drastic view to achieve the objective of the commerce clause? Apparently not. There seems to have been too much stress laid upon the label rather than upon the substance of the tax. The court should ask itself: Does the tax actually discriminate against interstate commerce? It should not be any more difficult to find an acceptable answer to this question here than in other situations that are considered on that basis. If the answer is in the affirmative, then the tax should be declared void, but there seems to be no good reason for doing so when the answer is negative, which it may very well be.<sup>36</sup>

*Summary of the Tests.* Interstate commerce usually can be made to pay its way, or almost do so, under the existing tests adopted by the United States Supreme Court if the tax law is skillfully drafted to meet these criteria. While one tax may be struck down, another achieving the same or a substantially similar result will be upheld, *e.g.*, a sales tax may be replaced by a use tax and a privilege tax based on net income may be renamed a net income tax. There are, however, the disadvantages of administrative complications and of differences in tax base to which allusion has been made. Perhaps worst of all is the problem of the time lag while counsel test their skill in securing rulings that a tax does or does not conform to criteria that often are more conceptualistic than practical in their actual operation. There can be fair and efficient state taxation under which interstate commerce will pay its way, no more, no less, if the tests now applied under the commerce clause are re-examined in the light of their economic incidence, and if the states

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*cal Program to Improve Taxation of Interstate Highway Use*, National Association of Tax Administrators (1952) and *Suggested Interstate Highway Use Tax Law*, Council of State Governments (1952).

<sup>35</sup> *Railway Express Agency, Inc. v. Virginia*, 347 U.S. 359 (1954).

<sup>36</sup> An illustration of the contradictory situations developing under state franchise tax laws is found in the recent decision of the Michigan Supreme Court in the case of *Panhandle Eastern Pipeline Co. v. Michigan Corporation and Securities Commission*, 77 N.W. 2d 249 (Mich.) (1956), in which the United States Supreme Court has denied certiorari. Notwithstanding prior recognition of the validity of state privilege taxes imposed on foreign corporations conducting both interstate and intrastate business within a state, *e.g.*, *International Harvester Co. v. Evatt*, 329 U. S. 416 (1947), in the *Panhandle Case* it was held that the commerce clause prohibited inclusion of receipts from the company's sales of gas transported into the state from out-of-state sources in the numerator of the sales factor used for apportionment purposes. The company had comparable sales of locally produced gas, and hence was engaged in both interstate and intrastate activity. Although state tax administrators are confining this holding to companies that are in situations that are identical, or nearly so, there has been inevitable confusion. There is pressing need for a clearer and more realistic approach to the problem.

cooperate with the Federal Government in developing laws and procedures thereunder that are designed to achieve this goal without indulging in distinctions that are so finely drawn that they tend to confuse rather than to clarify the issue.